Euler Hermes Economic Research

Country Report

Ireland

The Celtic Tiger has new teeth

General Information

GDP	USD232.08 bn (World ranking 45, World Bank 2013)
Population	5 mn (World ranking 120, World Bank 2013)
Form of state	Parliamentary Republic
Head of government	Enda KENNY (Fine Gael)
Next elections	2016, legislative

Strengths

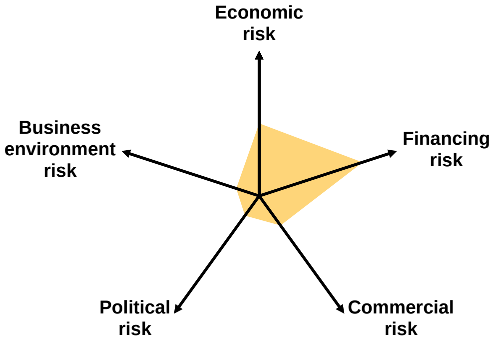
- Strong business environment
- Lowest corporate rate within the Eurozone
- Exports oriented towards sectors with high value added
- Robust current account surplus
- Strong education system
- English speaking business location

Weaknesses

- Sensitive to external shocks due to high openness
- Excessive private and public debt
- Low and long-lasting inflation

Country Rating

BB2



Source: Euler Hermes

Trade Structure

By destination/origin (% of total)

Exports		Rank		Imports
United States	21%	1	37%	United Kingdom
United Kingdom	15%	2	9%	Germany
Belgium	13%	3	8%	United States
Germany	8%	4	6%	Netherlands
France	6%	5	5%	China

By product (% of total)

Exports		Rank		Imports
Pharmaceuticals	25%	1	9%	Pharmaceuticals
Basic Organic Chemicals	22%	2	6%	Refined Petroleum Products
Toiletries	9%	3	5%	Computer Equipment
Miscellaneous Manuf. Articles	6%	4	5%	Basic Organic Chemicals
Precision Instruments	4%	5	5%	N.E.S. Products

Sources: Chelem (2013)

Economic Overview

Ireland is still an export-story but domestic demand bounces back

After a severe economic crisis, Ireland experienced in 2014 the fastest economic growth within the Eurozone: +4.8% - see Figure 1. Mainly driven up by exports (+12.6%), which contributed 2pps to 2014 GDP, and for the first time since 2007, domestic demand. This performance came from significant competitiveness adjustments over the past years thanks to ambitious labor market reforms and was boosted by the recovery in Ireland's main trade partners: the United States, the United Kingdom and Germany, accounting for almost half of total Irish exports. Going forward, we expect Irish exports to benefit from the lower euro given the high share of exports outside the Eurozone as well as the export structure, which is sensible to price variations.

Private consumption rebounded to 1.2% growth in 2014 (against -0.8% in 2013), as did total investment (+11.7%), while public spending growth softened (+0.2%). As the labor market reforms continue to bring new skills to the labor force while also increasing the flexibility of wage-setting within several sectors, both unemployment and employment continued to show improvement: in Q1 2015 employment increased to 2.2% y/y led by construction (19,600), industry (9,300), and financial services (4,600); while unemployment continued to fall (10.0% in March against 13.1% in 2013). Irish housing prices have been steadily increasing for over two years now, up 15.8% y/y in April, though largely from growing disparity between strengthening demand and lagging supplies (just 11,000 house completions in 2014). Domestic demand should gather pace following 2014's performance, helped by a better employment outlook, and notably high consumer confidence that is now at its highest point since early 2006 - see Figure 2.

Euler Hermes expects GDP growth to remain strong in the coming years at +3.7% in 2015 and +3.2% in 2016.

Good news for several sectors, but some weaknesses persist

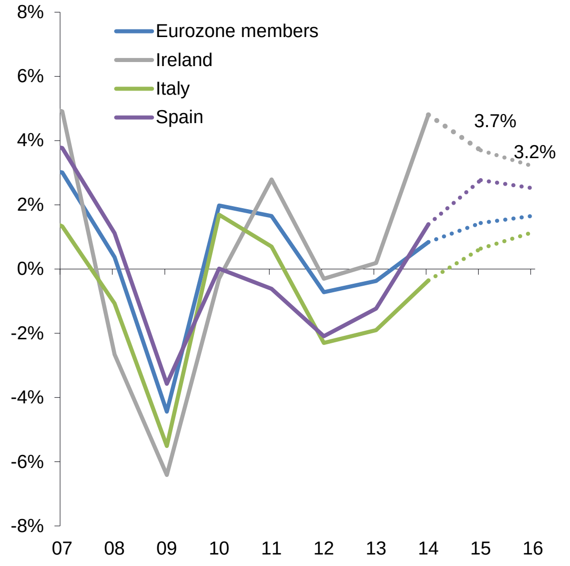
In addition to the lower euro, Irish corporates should benefit from lower oil prices and easier financing conditions as a result of the ECB QE program. Therefore, non-financial corporates' margins are expected to increase by +1.4pp to 56% of the value added (see Figure 4). The pass-through to the real economy is visible and several sectors have seen improvements in their risk profiles.

For example the Agrifood sector benefits from export diversification towards new and emerging markets, and the Pharmaceuticals sector gets support from the presence of several multinationals in Ireland thanks to the competitive fiscal regime. Combined with lower oil prices, this improvement has spillover effects on the Transport sector but also the Chemical sector. These are strongly linked to the Agrifood sector through fertilizer production, and which was upgraded from "medium risk" to "low risk" in Q4 2014. Going forward, even if the consumer-driven sectors (retail and household equipment) remain on the "watch list", they are expected to show some progress with the renewal of the domestic consumption.

Financial sector remains challenging

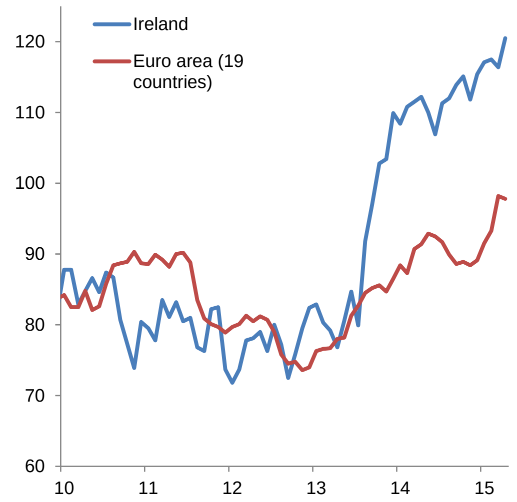
The banking sector has been almost entirely restructured and the results of the ECB Asset Quality Review (AQR) and the EBA stress test brought the necessary investor confidence following broadly positive results. All Irish based institutions passed the AQR and stress tests under the baseline scenario, and all but one passed under their adverse stress scenario. However, the implementation of new capital requirements will prove challenging, as bank profitability remains low - Ireland's two largest banks (BOI and AIB) only just turned their first profits since the financial crisis last year. Further weighing on bank profitability, the share of non-performing loans and

Figure 1 GDP growth



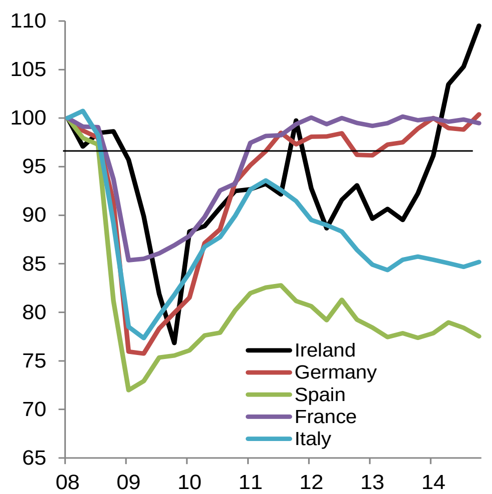
Sources: IHS, Euler Hermes forecasts

Figure 2 Consumer Confidence Index



Sources: Eurostat, Euler Hermes

Figure 3 Non-financial firms' turnovers, Q1 2008 = 100



Sources: Eurostat, Euler Hermes

incidence of mortgage arrears remains high: (1) non-performing loans still represent about 23% of the total. This is one of the highest rates in the EU. It is also an impediment to the capacity of banks to support the economic recovery; (2) mortgage arrears (above 90 days) sat at 9.8% in Q1 2015, against 3.3% in Q3 of 2009, while repossessions have steadily increased, up 51% when compared to a year earlier.

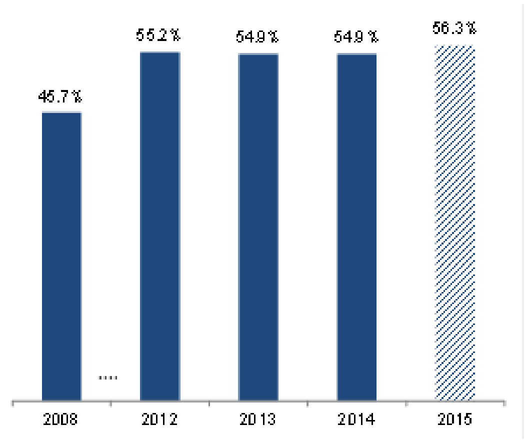
Private and public sector debt remain excessive, but appear to be heading in the right direction

Household debt has been steadily declining since a peak of EUR 203bn in Q3 of 2008, falling to EUR 157 bn in Q4 2014, or roughly EUR 34 thousand per capita. Debt as a proportion of disposable income has fallen as well, now 173% (against a high of 216% in Q2 2011), which is the lowest ratio since mid-2005. However, this still remains high when compared to other Eurozone members. Current levels put Ireland below only Denmark and Netherlands, while above neighboring UK's high (170% - pre crisis). Meanwhile, debt as a percentage of household assets is declining at a faster pace than the reduction in debt itself, indicating gains from appreciation of Irish household assets and the improvement in the financial stability of Irish families (see Figure 5).

2015 will mark a third consecutive year of falling business insolvencies, but they are still 3 times higher than in 2007

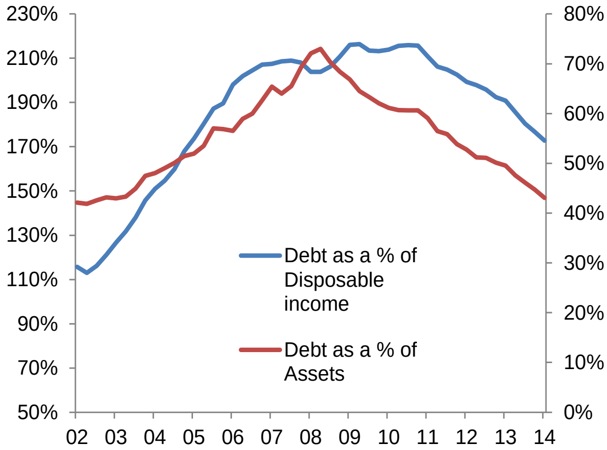
Against this background, business insolvencies are expected to decline for the third consecutive year (-9% in 2015 and –8% in 2016) - see Figure 6 - after -15% in 2014. The Q1 2015 is already showing good results with a -17% decline compared to Q1 2014. However, despite this fall the total level of insolvencies in 2015 will remain three times higher than in 2007, especially in the construction sector which suffered from the housing market crisis and accounted for 24% of total insolvencies in 2014.

Figure 4 Non-financial firms' margins, % of value added



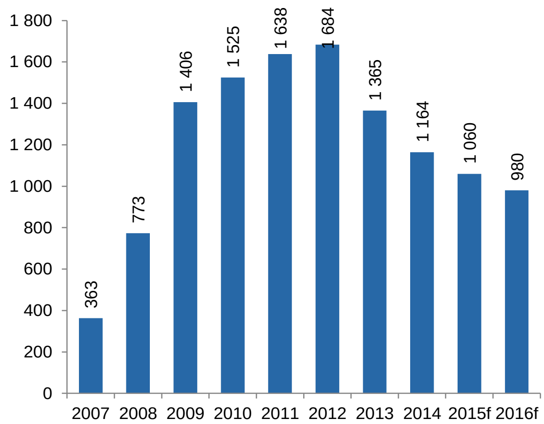
Sources: Eurostat, Euler Hermes

Figure 5 Private Debt ratios



Sources: National Sources, Euler Hermes

Figure 6 Business insolvencies (number)



Sources: National Sources, Euler Hermes

Last review: 2015-06-16
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